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CASE NO. 80-1188

IN THE

SUPREME COURT OF THE UNITED STATES

OCTOBER TERM, 1981

JAMES EDGAR,

*Appellant,*

v.

MITE CORPORATION, and
MITE HOLDINGS, INC.,

*Appellees.*

ON APPEAL FROM THE UNITED STATES
COURT OF APPEALS FOR THE SEVENTH CIRCUIT

# BRIEF OF THE STATE OF OHIO AS AMICUS CURIAE

**WILLIAM J. BROWN**
*Attorney General of Ohio*

**ROGER P. SUGARMAN**
*Assistant Attorney General*

*State Office Tower*
*30 East Broad Street, 16th Floor*
*Columbus, Ohio 43215*
*(614) 466-8614*

**ATTORNEYS FOR THE**
**STATE OF OHIO**
**AS AMICUS CURIAE**

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## INTEREST OF THE STATE OF OHIO

The State of Ohio, by and through the Commissioner of the Ohio Division of Securities, is statutorily charged with the responsibility for the regulation and enforcement of the Ohio Securities Act, including the provisions of the Ohio Takeover Statute (the "Ohio Act"), Section 1707.041 of the Ohio Revised Code. As the second state to enact a statute regulating corporate acquisitions by tender offer, Ohio extends protection to investors by requiring that shareholders confronted by a tender offer be provided with fair, full and effective disclosure of all information material to a decision to accept or reject the offer.

This case concerns the validity of the Illinois Business Take-Over Act, Ill. Rev. Stat. ch. 121 ½ section 137.51 et seq. (1979) (the "Illinois Act"), and its application to a proposed corporate acquisition by tender offer. This transaction was subject also to the provisions of the Williams Act amendments to the Securities Exchange Act of 1934 (the "1934 Act"), 15 U.S.C. 78m(d)-78m(e), 78n(d)-78n(f), the parallel federal regulation governing tender offers. The United States Court of Appeals for the Seventh Circuit concluded that the Illinois Act is preempted by the Williams Act; the Illinois Act burdens interstate commerce; and therefore, the Illinois Act is unconstitutional. The Seventh Circuit did not believe, however, that all state legislation in this field was unconstitutional, nor did it see any reason that the Williams Act could not be validly complemented and investor protection furthered by state takeover statutes.[1]

The resolution of the complex constitutional issues presented by this case may have a substantial impact upon the continued protection of investors through the operation of the analogous Ohio Takeover Act and its administration by the the Commissioner of the Ohio Division of Securities. The State of Ohio respectfully submits this brief in support of (a) the constitutionality of the Illinois Act, and (b) the conclusion shared by the Seventh Circuit that not all state regulation of tender offers is unconstitutional *per se*. The brief includes an analysis of the practical effect of the Ohio Act as it has been interpreted and applied, to demonstrate that state statutes serve to complement and effectuate the investor protection purpose of the Williams Act without placing excessive burdens upon interstate commerce.[2]

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1. *Mite Corporation v. Dixon*, 633 F.2d 486, 502-3 (7th Cir. 1980).

2. *See, AMCA International Corporation v. Krouse*, 482 F. Supp. 929 (S.D. Ohio 1979).

## SUMMARY OF ARGUMENT

I

State takeover statutes and their federal counterpart, the Williams Act, share identical purposes in the regulation of tender offers – the protection of investors. Each regulatory scheme effectuates its purpose through mechanisms which are designed to provide disclosures to shareholders of target corporations, upon which the shareholders may then make informed investment decisions. While the statutory schemes are not procedurally identical, the state statutes complement and are consistent with the Williams Act, rather than being in conflict.

Congress has not expressly preempted state regulation of tender offers in either the Securities Exchange Act of 1934 or the Williams Act amendments thereto. On the contrary, Section 28(a) of the 1934 Act specifically preserves state laws insofar as those laws do not conflict with the provisions of the 1934 Act.[3] Furthermore, there is no exclusive federal occupation of the field of securities regulation from which congressional preemption of state takeover statutes can be inferred.

Rather, this is a case like *New York Dept. of Social Services v. Dublino,* 413 U.S. 405, 421 (1973), in which

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3. As noted by the Seventh Circuit, 633 F.2d at 499, n.25, the Securities and Exchange Commission promulgated Rule 14d-2(b), 17 C.F.R. 240. 14d-2, effective January 7, 1980. If valid, the effect of Rule 14d-2(b) would be to preempt the precommencement public announcement provisions of virtually all of the thirty-seven (37) state takeover statutes presently in existence. The validity of this Rule and its effect upon the Ohio Takeover Act is currently *sub judice, Canadian Pacific Enterprises (U.S.) Inc. v. Kenneth E. Krouse* (No. 81-3083, 6th Cir., *appeal pending*). Rule 14d-2(b) did not apply to the controversy before the Seventh Circuit and that court did not consider its effect upon the Illinois Act. Accordingly, this brief will not address the validity or effect of Rule 14d-2(b), but will consider the merits and facts of the controversy as determined by the Seventh Circuit.

this Court declined to preempt state law "[w]here coordinate state and federal efforts exist within a complementary administrative framework, and in the pursuit of common purposes. . . ." Existing within this complementary framework, state takeover statutes such as that of Illinois do not stand as an obstacle to the accomplishment and execution of the purposes and objectives of the Williams Act, *Hines v. Davidowitz*, 312 U.S. 52, 67(1941), and are therefore constitutional.

## II

State takeover statutes recognize that tender offers are unique transactions which combine elements of corporate transactions traditionally regulated by the states, and elements of securities transactions traditionally subject to cooperative federal-state regulation. A tender offer represents a change in and acquisition of corporate control, a process which the states have a legitimate interest in regulating for the purpose of protecting the investor/shareholder, as with similar internal affairs transactions of corporations.

These state statutes further other legitimate state interests which, when balanced against alleged burdens resulting from compliance therewith reveal that no impermissible burden upon interstate commerce exists. So too, this balancing process affirmatively demonstrates that any burden upon interstate commerce attributable to state takeover statutes is not "clearly excessive" in relation to their identifiable and substantial legitimate state interests.

## ARGUMENT

### I

### PROTECTION OF INVESTORS, THE SOLE PURPOSE OF THE WILLIAMS ACT, IS CONSTITUTIONALLY COMPLEMENTED AND FURTHERED BY STATE TAKEOVER STATUTES.

The United States Court of Appeals for the Seventh Circuit determined that Congress did not expressly preempt state regulation of tender offers in either the Securities and Exchange Act of 1934 or the Williams Act amendments thereto and affirmatively concluded that such federal legislation did not "bar the states from regulating tender offers." 633 F.2d 486 at 491. Similarly, in response to the argument that preemption of state regulation in this area may be inferred, the Court stated that:

> Nor is the federal scheme of regulating tender offers so pervasive that an implicit congressional intent to preempt parallel state legislation may fairly be inferred. *Id.* at 491.

Rather, the Seventh Circuit found "the absence of an exclusive federal interest in the field of securities regulation [to be] persuasively demonstrated by the historically coordinate role of state regulation in the field." *Id.* The Court of Appeals, however, in applying the "conflict" test of *Hines v. Davidowitz*, 312 U.S. 52 (1941), coupled with the rationale of *Great Western United Corp. v. Kidwell*, 577 F.2d 1256 (1978), *rev'd on venue grounds sub nom. Leroy v. Great Western United Corp.*, 443 U.S. 173 (1979), did conclude that the Illinois Act is preempted by the Williams Act. 633 F.2d at 498.

Inquiry into the existence of "conflict" under the *Hines* test requires that a court "consider the relationship between state and federal laws *as they are interpreted and applied, not merely as they are written.*" (Emphasis added). *Jones v. Rath Packing Co.*, 430 U.S. 519, 526 (1977). Yet the Seventh Circuit, by its own admission was unable to do so, for:

> . . . any conslusion as to the actual effect it [Illinois Act] has had, or may have, on tender offers in Illinois would be purely speculative because the record is devoid of evidence on that subject. 633 F.2d at 497.

Thus, the Illinois Act which was neither applied to nor operative in the Mite-Chicago Rivet tender offer; of which no prior history or experience was contained in the evidentiary record; and, as to which conclusions based upon speculation were made, was found to somehow be an obstacle to the accomplishment and execution of the purposes of the Williams Act.

By way of contrast, the Ohio Act, after ten years of existence; actual application to sixteen (16) tender offers; and, three days of trial in federal district court based upon its history and application, was held not to have been preempted by the Williams Act. *AMCA International Corp. v. Krouse*, 482 F.Supp. at 938 (1979) (hereinafter referred to as *"AMCA"*). While the Ohio and Illinois Acts are parallel rather than identical, they share a mutuality of purpose which when examined (as in *AMCA*), reveal that state takeover statutes effectively complement the Williams Act, benefit shareholders and protect investors.[4] The unique and extensive

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4. This Court in *Piper v. Chris-Craft Industries, Inc.*, 430 U.S. 1, 35 (1977), after reviewing its legislative history, definitively stated that "the *sole purpose* of the Williams Act was the *protection of investors* who are confronted with a tender offer." (Emphasis added). Illinois and Ohio share this identity of purpose in their respective takeover statutes.

application and history of the Ohio Act, together with the analysis thereof by the *AMCA* court, demonstrate the shortcomings of the Seventh Circuit's corresponding analysis of the Illinois Act.

Ohio has been the most active state to date in terms of filings and proceedings under its takeover statute, to determine whether "the offeror proposes to make fair, full and effective disclosure to offerees of all information material to a decision to accept or reject the offer." R.C. 1707.041(B)(1)(c).[5] This dominant theme of investor protection through disclosure mirrors the efficacy and desirability of disclosure as revealed by the legislative history of the Williams Act [H.R. Rep. No. 1711, 90th Cong., 2d Sess. 2813 (1968)], and reaffirmed by this Court in *Rondeau v. Mosinee Paper Corp.*, 422 U.S. 49, 58 (1975). The possibility that disclosure to shareholders/investors would deter the making of a tender offer was considered and dismissed during deliberations upon the Williams Act [H.R. Rep. No. 1711 at 2813-14], and is belied by the experience in Ohio which has demonstrated "that tender offers have [not] been unduly inhibited by the Ohio Act." *AMCA* at 938.

The Williams Act was characterized by the Seventh Circuit as "essentially a minimum disclosure statute." 633 F.2d at 491. The Ohio Act adds flesh to this federal skeleton of investor protection through disclosure, so as to differ therefrom primarily in that it:

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5. Disclosure to offeree/shareholders was also the means selected in the Williams Act for protection of investors, as evidenced by the following statement by the Act's sponsor, Senator Williams:

> This legislation will close a significant gap in *investor protection* under the Federal securities laws by requiring the *disclosure* of pertinent information *to stockholders* when persons *seek to obtain control of a corporation* by a cash tender offer or through open market or privately negotiated purchases of securities. 113 Cong. Rec. 854 (Emphasis added.)

> . . . requires fuller disclosure, imposes administrative review, extends the period of public scrutiny and requires that the tender offer be made on the same terms to Ohio shareholders as to others. *AMCA* at 936.[6]

"Fuller disclosure" provides information material to the shareholder's decision, so that acceptance or rejection of the offer may then be made intelligently upon evaluation of these disclosures by the shareholder.[7] This is especially relevant to the shareholder who may wish to remain a shareholder rather than tender, or in the event that a tender offer is made for less than all of the outstanding securities of a corporation.

Disclosure to investor/shareholders is also a product of the "administrative review" procedures undertaken by the Ohio Division of Securities (the "Division") if hearings are conducted in accordance with the Act. R.C. 1707.041(B)(1). Administrative hearings are held to test

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6. The operative language of the Ohio Statute requires and provides, *inter alia:* (i) 20 days prior to a takeover bid, the offeror must publicly announce the terms of the offer; (ii) at the same time, file with the Division of Securities and the target company copies of information required by R.C. section 1707.041(B)(3); (iii) administrative hearing to review the offer when ordered by the Division or requested by the target and the Division so orders, either of which must occur within 10 days of the filing; (iv) if a hearing is ordered it must be held within 40 days of the date of the filing; (v) adjudications made pursuant to hearing must be made within 60 days of the date of filing; and, (vi) if no hearing is ordered, the offeror may proceed at the end of the 20-day period from the date of the initial filing.

7. *E.g.,* R.C. 1707.041(B)(3)(g) and (h) require an offeror to disclose its capitalization, financial statements, pending non-routine litigation, etc. .... *AMCA* at 936. Disclosures in the Occidental Petroleum tender offer for Mead Corporation included, as a result of proceedings in Ohio, potential problems of Occidental (offeror) with its Hooker Chemical subsidiary and with the Libyan government.

the adequacy of the disclosure materials proposed to be disseminated to shareholders, with ultimate discretion resting with the Division as to convening a hearing.[8] Adjudications made pursuant to the hearing process, again, have focused upon the adequacy of the offeror's disclosures, to determine whether they are fair, full and effective.[9]

Moreover, the practical effect of evaluation of the disclosures under the Ohio Act has been to create sufficient time within which a shareholder may assess the offering documents in order to reach an informed investment decision. This "delay" prevents a "knee-jerk" response by a shareholder to an offer that is made at a premium over the then-prevailing market price of the target company's stock, without having had an opportunity to digest and evaluate complex disclosure materials provided pursuant to federal and state law. State takeover statutes establish a readily ascertainable time schedule within which the investor, the investment community and the stock markets may adjust to and react to the volitility caused by a theretofore unannounced tender offer.

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8. A target company may not automatically convene a hearing before the Division upon its request. The Division is the ultimate arbiter in this regard and has refused to convene hearings even though requested to do so. *AMCA* at 494. *Compare,* Ill. Rev. Stat. ch. 121 ½, Section 137.57.A.

9. Similar to Ill. Rev. Stat. ch. 121 ½ Section 137.57.E, the Ohio Act provides for a "fairness" review of a tender offer by the Division. R.C. 1707.041(B)(4). No such review of the fairness of a tender offer has ever been undertaken or made under the Ohio Act, nor has the Division ever ordered that an offeror could not proceed wth its offer. The hearing process *has* resulted in additional disclosures to shareholders and the process and adjudication have *always* been completed within the prescribed statutory time of sixty (60) days from date of filing.

The natural result of this process has been the creation of a bidding market in the shares of the target company's stock, as the market is thus able to assess the disclosures of the offer and their adequacy and thereby respond in a responsible fashion. The benefits which inure to the investor/shareholder therefrom have been numerous. The investor who desires to make an immediate liquidation has a market during the offering period (at or near the tender offer price), as neither state nor federal law preclude the ability to sell on the open market. Or, the investor may wait until the best price is developed in the marketplace as the result of a competing tender offer. This latter phenomena would oftentimes not occur, but for the existence of state takeover statutes.[10] The evolvement of this market and its attendant inarguable benefits to shareholders serve to best-exemplify the investor protection philosophy and reality embodied by state takeover statutes.

The record in *AMCA* of the history and application of the Ohio Act conclusively establishes that Ohio has mirrored the disclosure policy of the Williams Act, yet has supplemented and complemented the minimum federal requirements to successfully achieve investor protection. The application and interpretation of the Ohio Act simply belies the pejorative label attached to state takeover statutes, that they have adopted a "fiduciary" rather than a "market" approach to

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10. This increase in the price paid is most dramatically demonstrated by the market created during the tender offer of AMCA International Corporation for Warner & Swasey. Because of the "braking effect" which the Ohio Act had upon AMCA's actions, Bendix Corporation, a competing offeror, was able to enter the contest. AMCA's original offer was at $57.00 per share at a time when Warner & Swasey's stock was valued in the market at about $36.00 per share. When Bendix ultimately acquired Warner & Swasey, the price paid per share was $83.00, after AMCA had increased its offer to $75.00 per share in response to Bendix's initial competing offer of $70.00 per share. This represented an aggregate increase of more than $90 million to Warner & Swasey shareholders.

regulation of tender offers.[11] The ultimate arbiters of every tender offer subject to the Ohio Act and the jurisdiction of the Division have been the investor/shareholders. *AMCA* at 938. The Ohio Act was designed to and has in fact protected these beneficiaries of the statute by providing a reasonable period of time within which to reach an informed investment decision and to assess the reaction of the market to the offer.

The relationship of the Williams Act and parallel state regulation, as interpreted and applied to the experience and history of the Ohio Act by the court in *AMCA International Corp. v. Krouse,* 482 F.Supp. 929 (S.D. Ohio 1979), affirmatively supports the Seventh Circuit's belief that it is "possible to draft state takeover legislation to supplement (rather than to contradict) the Williams Act and the congressional *premises and purposes which it incorporates.*" 633 F.2d at 503. The Ohio Act further offers empirical evidence for the Seventh Circuit's perception that "the Williams Act may ... be validly complemented and investor protection furthered by state legislation." *Id.*

11. The lable that the Illinois Act adopts a "fiduciary approach" is similarly unfounded, as the record below does not examine the application or interpretation of that Act, but simply reviews the facial wording of the Act. 633 F.2d at 497.

## II

## THE REGULATION OF INTERNAL CORPORATE AFFAIRS BY STATE TAKEOVER STATUTES TO EFFECTUATE INVESTOR PROTECTION DOES NOT VIOLATE THE COMMERCE CLAUSE OF THE UNITED STATES CONSTITUTION.

The Seventh Circuit, utilizing the balancing test formulated in *Pike v. Bruce Church, Inc.*, 397 U.S. 137, 142 (1970), also concluded that the Illinois Act violates the Commerce Clause of the United States Constitution. It did so, despite the absence of an evidentiary record against which the actual operation of the Illinois Act could be compared. While the Court's analysis refers to "potentially weighty" burdens; "significant potential" of the Act to cause commercial disruption; and "no evidence in the record as to what the actual effect of the Act" has been in preventing the removal of local business from Illinois; the Court is nevertheless firm in its conviction that "the Illinois Act burdens interstate commerce in a manner which is *substantial, clear* and *present* . . . ." 633 F.2d 502-503 (Emphasis added).

The Illinois Act is, *inter alia*, a state statute designed to regulate the internal affairs of a corporation which has a sufficient nexus to the State of Illinois.[12] Although the statute serves other legitimate local interests, the Act seeks to regulate significant corporate changes which inexorably result from a successful tender offer. As corporations are creatures of state law, the states have traditionally regulated significant structural changes

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12. This nexus is met if a corporation, *inter alia*, meets any two of the following conditions: (a) principal executive office in Illinois; (b) organized under the laws of Illinois; (c) at least 10% of its stated capital and paid-in surplus represented in Illinois. Ill. Rev. Stat. ch. 121 ½, Section 137.52-10.

which occur when control of the corporation shifts.[13] The legislative history of the Williams Act also recognizes that tender offers are unique transactions, unlike any other transfer of securities.[14]

Once again, the analysis by the *AMCA* court of the detailed evidentiary record of the history and application of the Ohio Act is helpful for purposes of a commerce clause analysis.[15] The Court found the Ohio Act to regulate evenhandedly the conduct of offerors. 428 F.Supp. at 938. More importantly, however, the Court believed, upon the facts before it, that Ohio had "abundant legitimate public interest" regulating a proposed tender offer for Warner & Swasey. *Id.* at 939.[16] This interest was premised upon the court's recognition that:

> Tender offers profoundly affect corporate internal affairs and fiduciary relationships traditionally within the purview of state regulation ... tender offers are to be considered functionally as internal affairs transactions, comparable to proxy contests and mergers, in which a state possesses a compelling interest: investor protection. *Id.*

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13. *Cort v. Ash*, 422 U.S. 66, 84 (1975). In addition to *Cort v. Ash*, this Court's decision in *Santa Fe Industries v. Green*, 430 U.S. 462 (1977) dispels any notion of a dominant federal interest in the regulation of corporations. Taken together, these decisions emphasize the cooperative nature of federal-state regulation of securities transactions generally, and primary deference to state law regulating the internal affairs of a corporation specifically.

14. Senate Comm. on Banking and Currency, *Full Disclosure of Corporate Equity Ownership in Corporate Takeover Bids*, S. Rep. No. 550, 90th Cong., 1st Sess. 2-4 (1967).

15. The jurisdictional nexus of the Ohio Act requires that a corporation be organized under the laws of Ohio or have its principal place of business and substantial assets within Ohio. R.C. 1707.041(A)(1).

16. Warner & Swasey was an Ohio corporation with its principal place of business in the State, as well as the main part of its assets and approxiately one-third of its shareholders in Ohio. *Id.*

See, Shipman, *Some Thoughts About the Role of State Takeover Legislation: The Ohio Takeover Act,* 21 Case W. Res. L. Rev. 722, 741-45 (1970).

The fact that a statute may have effect beyond the boundaries of the state does not make such statute invalid under the Commerce Clause. The allegation of "extraterritoriality" is particularly anomalous when state corporation law, by its very nature, extends beyond the boundaries of the regulating state. Accordingly:

> ... it is a curious suggestion that extraterritorial protection of shareholders is illicit in the context of state tender offer statutes, but expected in the context of state corporation laws. Note, *The Constitutionality of State Takeover Statutes: A Response to Great Western,* 53 N.Y.U. L.R. 872, 922 (1978).

Therefore, any extraterritorial effect of state takeover statutes must first be shown to be a burden and then weighed against the legitimate state interests fostered by the statute before it can be concluded that the alleged burden on interstate commerce is "clearly excessive" in relation to the statute's benefits.

The case at bar illustrates the compelling interest of the State of Illinois in protecting investors by the Illinois Act's regulation of the proposed change in control of Chicago Rivet to Mite Corporation. Chicago Rivet is organized under the laws of the State of Illinois and has its principal executive office in Illinois. Additionally, the Seventh Circuit determined that approximately 27% of Chicago Rivet's shareholders were Illinois residents, which represented approximately 43% of the outstanding shares. 633 F.2d at 501. Thus, as the controlling forum of the internal affairs of an Illinois corporation, the

legitimate interests of the State of Illinois in exercising regulatory authority in a tender offer for Chicago Rivet cannot be gainsaid.[17]

In light of these legitimate state interests and without the benefit of a record evidencing the application of the Illinois Act, it is unlcear how the Illinois Act was found to impose upon interstate commerce a burden that is "clearly excessive in relation to the putative local benefits." *Pike v. Bruce Church, Inc., supra* at 142. Any perceived or alleged burden is not demonstrated by the record, but rather exists in theory and speculation.[18] By contrast, the examination of the Ohio Act in *AMCA* illustrates the exacting scrutiny of the actual application of a state statute under the *Pike* balancing test and commerce clause analysis. Having done so, the court found "the Ohio Act, like any regulation, affects commerce and imposes costs upon regulated parties." 482 F.Supp. 941. Yet having *reviewed the record,* the court concluded that the Ohio Act did not impose an impermissible burden upon interstate commerce. *Id.*

When appropriately viewed as the regulation of internal corporate affairs to effectuate investor protection, state takeover statutes exist well within the bounds of any commerce clause guidelines. Such legitimate, even compelling, local interests of the states

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17. The Seventh Circuit clearly recognized that "[p]rotecting resident investors is indisputably a legitimate state objective." *Id.* at 500. The Court, however, absent an evidentiary record, concluded that "the benefits flowing to Illinois shareholders from the Act are, to a significant degree, speculative." *Id.*

18. For example, the history of tender offers to date does not support the Seventh Circuit's fear that a multitude of states will impose conflicting regulations on an offeror through their respective tender offer statutes. 633 F.2d at 502. To the contrary, the tender offer of United Technologies for Babcock and Wilcox exemplifies state cooperation, whereby the New Jersey authorities relied upon testimony produced in Ohio hearings for review under the New Jersey takeover statute. In the case at issue, while it was alleged that two states could have asserted jurisdiction, in fact, only Illinois did.

do not burden commerce in relation to the putative local benefits. Rather, they preserve recognized fiduciary relationships between shareholders and corporate management. When afforded their appropriate deference in the balancing test, such state interests clearly outweigh any potential burdens which result from compliance with state takeover statutes.

## CONCLUSION

For the foregoing reasons, the judgment of the United States Court of Appeals for the Seventh Circuit should be reversed.

Respectfully submitted,

**WILLIAM J. BROWN**
*Attorney General of Ohio*

**ROGER P. SUGARMAN**
*Assistant Attorney General*

*State Office Tower*
*30 East Broad Street, 16th Floor*
*Columbus, Ohio 43215*
*(614) 466-8614*

**ATTORNEYS FOR THE STATE OF OHIO AS AMICUS CURIAE**

Dated: July 17, 1981.